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SUBJECT: 2006 NTE UPDATE FOR BULGARIA

¶1. The following is Embassy's input for the 2006 National Trade Estimate (NTE) report for Bulgaria. The text -- including the ranking of barriers -- has been sent electronically to USTR and State (EB).

RANKING OF BARRIERS: The following are general range estimates of what the increase in U.S. exports to Bulgaria would be if barriers were removed:
--FAS-Sofia estimates losses in potential U.S. agricultural-related exports at USD 10-15 million due to the applied trade regime. Tariffs and tariff rated quotas cause losses of about USD 10 million for poultry and about USD 5 million for pork products.
--The Association of American Pharmaceutical Companies in Bulgaria (AAPCB) estimates that if barriers to trade were eliminated for U.S. pharmaceutical imports, increased annual imports would be about USD 10-25 million. AAPCB estimates the pharma-economic analysis used in composing the positive list could result in an additional loss for American Pharmaceutical Companies of USD 15-20 million. Three US companies (Merck, J&J and Pfizer) estimate that the reduction of the patent life of their innovative medical products in violation of international standards would result in a loss of USD 29 million over the next two years;
--The Business Software Alliance (BSA) estimates losses to U.S. producers of business applications at USD 16 million for 2004, with a piracy rate of 71 percent;.
--A U.S. information technology (IT) company (Microsoft) estimates that if the Bulgarian government eliminated administrative barriers to the sale of its products and adequately protected IPRs its overall exports to Bulgaria could increase more than four times or by USD 80-100 million;
--U.S. Recording Industry representatives estimate that losses from sales in Bulgaria of pirated/smuggled CDs were USD 6.5 million in 2004;
--An American insurance firm estimates that a lifting of government procurement barriers for insurance could generate contracts worth USD 10-25 million (about 25 percent of the market);
--The Distilled Spirits Council of the United States (DISCUS) maintains that high tariffs on U.S. distilled spirits encourage smuggling and counterfeiting (we do not have an estimate for such losses, but place it under USD 10 million);

(Note: In general, increased exports if barriers were removed are hard to quantify. U.S. investments also draw U.S. exports, so problems with the investment climate spill over to export potential. The following are some general matters negatively affecting U.S. exports to Bulgaria:
-- The 2005 constitutional amendment on foreign individuals' property rights in Bulgaria favors EU over U.S. investors and puts US citizens at disadvantage;
-- U.S. investors are disadvantaged by not having an avoidance of double taxation agreement with Bulgaria.

TEXT OF NATIONAL TRADE ESTIMATE SUBMISSION

Begin Text

BULGARIA

TRADE SUMMARY

((To be provided by USTR))

IMPORT POLICIES

Tariffs

Bulgaria's trade policies are shaped primarily by its World Trade Organization (WTO) membership and by its status as a candidate for EU membership. Bulgaria has a preferential trade agreement with the European Union (EU) under its Europe Agreement, and free trade agreements with the European Free Trade Area (EFTA) countries. It also has free trade agreements with its Central European neighbors (CEFTA), Turkey, Macedonia, Albania, Serbia and Montenegro, Bosnia and Herzegovina, Israel and Moldova.

Upon accession to the EU, Bulgaria will be required to renounce its Europe Agreement and the other free trade agreements, and to align its tariffs with those of the EU. US exporters/investors will benefit overall from Bulgaria's EU accession since Bulgaria will join the EU's trade policy regime - a single set of trade rules and customs procedures. US exporters will benefit from lower tariffs as well. Average most favored nation (MFN) tariff rate, for example, would come down from its current level of 11.55 percent to an average of 6.5 percent.

For 2005, Bulgaria's average import tariff is 11.48 percent; the average level for industrial goods is 8.58 percent and the average level for agricultural goods is 22.89 percent. The maximum ad valorem level for agricultural goods, which is applied on 0.38 percent of tariff positions, is 75 percent. Bulgaria has eliminated all tariffs on industrial imports from the EU under its association agreement with the European Union. Industrial exports to Bulgaria from the rest of the world face tariffs following their approval, expected in mid-December. (Note: Post will provide information on Bulgaria's 2006 customs tariffs following their approval, expected in mid-December.

Bulgaria's agricultural trade regime is characterized by high MFN tariffs, particularly for red meat and poultry, and by preferential agreements with the EU and CEFTA. Ad valorem duties and minimum customs charges of more than 100 percent serve as incentives for smuggling and fraud. Cargoes are often improperly identified, and falsely labeled and declared in an effort to avoid customs charges. The Bulgarian customs service also uses minimum import prices, which appear to be applied arbitrarily, to calculate customs duties, particularly on poultry shipments.

FOREIGN TRADE BARRIERS

Bulgaria provides the EU with preferential tariff rates and reciprocal duty elimination on numerous agricultural products, as well as on wine. These preferences are hurting U.S. agricultural exporters who face higher MFN rates. In particular, the high import tariffs favor Bulgaria's inefficient domestic chicken and pig meat industries. Import tariffs on U.S. chicken are 68 percent, with frozen cut parts subject to a 74 percent tariff.

The U.S. Government is currently reviewing Bulgaria's continued eligibility for the U.S. Generalized System of Preferences (GSP) program in view of the preferential treatment it affords to the EU. The U.S. has urged the Bulgarian government to lower MFN tariffs on a range of items to reduce the tariff differential and its negative effect on U.S. commerce.

Non-tariff Barriers

In general, customs regulations and policies are reported to be cumbersome, arbitrary and inconsistent. Problems cited by U.S. companies include excessive documentation requirements, slow processing of shipments, and corruption.

Bulgaria uses the single customs administrative document used by EU members.

STANDARDS, TESTING, LABELING AND CERTIFICATION

The registration processes for pharmaceutical products and for drug pricing and reimbursement, including the process by which the National Health Insurance Fund classifies drugs, are cumbersome and non-transparent. Newer drugs are often arbitrarily classified with their older, generic versions for pricing purposes, thereby limiting companies' ability to recover their research and development costs.

Although the Bulgarian Drug Agency (BDA) has made progress in bringing the process of registration closer to the EU requirements, Bulgaria still requires batch control for each individually imported batch and does not allow for an inspection of the foreign production site.

Today U.S. and other foreign pharmaceutical companies consider that Bulgarian pricing and reimbursement decisions are not based on objective and verifiable criteria as required by WTO and EU principles. In addition, no appeal procedures for government pricing and reimbursement decisions and no timeframes for reimbursement are provided in the Bulgarian law.

The Bulgarian price approval system hampers the ability of foreign companies to compete effectively, as the regulations impose the lowest registered price of the EU member states and do not allow companies to recover importation costs. In addition, price regulations provide for a tacit refusal of reimbursement, which is against EU legislation. Bulgaria's bureaucratic

reimbursement process requires multiple approvals, lacks objective criteria, and does not provide for an appeals process.

Health care providers and pharmaceutical industry representatives criticize the government's prescription drug coverage policy for its complicated and lengthy selection process, inappropriate criteria, inconsistent methodology, and susceptibility to corruption.

The Bulgarian government's drug supply mechanism constitutes a major market access barrier to pharmaceutical companies' exports. Under the new drug legislation, pharmaceutical companies are required to commit to pay any liquidated damages in case a distributor fails to supply the right medicine. Thus, the burden of responsibility for distributors is being shifted from the government to the pharmaceutical industry.

GOVERNMENT PROCUREMENT

Bulgaria is an observer but not a signatory to the WTO Agreement on Government Procurement (GPA). In its accession to the WTO, Bulgaria committed to accede to the GPA and to submit an offer by June 1997 and complete negotiations by December 1997. However, the Bulgarian government did not initiate the process for GPA accession until 2000, and has not yet submitted an offer. Upon its accession to the European Union, Bulgaria will be required to comply with the GPA.

Although Bulgaria's government procurement legislation underwent a substantial reform in 2004 to align the system with WTO and EU rules, bidders still complain that tendering processes are unclear - and subject to irregularities and corrupt practices, and court appeals are long and cumbersome.

Even though the goal of the 2004 Public Procurement Law was to introduce a more efficient, transparent and accountable system for public procurement, the business community considers it deficient in a number of areas. The law transferred procurement appeals from the administrative to the civil procedure and introduced an Arbitration Court under the Ministry of Economy and Energy. This quasi-arbitration is not popular among businesses, because out-of-court dispute resolution is new to Bulgaria and because all bidders have to agree to join the arbitration. However, the biggest obstacle stems from the fact that an appeal that is essentially administrative is to be resolved through a civil procedure.

The Bulgarian government has prepared amendments to the 2004 Public Procurement Law in order to incorporate new European legislation in the area of public procurement and further streamline the national procurement process. The law, however, offers little in the area of court appeals and has yet to be approved.

The Bulgarian government supported by the US Government succeeded in energizing the state Public Procurement Agency. Its management capacity and communication with businesses and the judiciary has increased significantly over the last year. However, its capacity to provide methodological guidance to government and essential non-central government entities such as hospitals, universities, municipalities, etc. is not sufficiently developed.

Defense procurement activities are subject to a lack of transparency and corrupt influences, and fail to comply with international standards. The purchasing, pricing, and reimbursement processes for drugs under Bulgaria's national health system are not transparent. The government can use the price-approval mechanism to regulate the market for any product, and bureaucratic barriers can limit patients' access to new products.

Government procurement practices in the energy sector appear to disadvantage foreign insurance companies. According to U.S. industry, procedures for awarding insurance contracts for companies within the energy sector are not transparent.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

In May 2004, Bulgaria was placed on the Special 301 Watch List for the first time in five years. The 2005 US government inter-agency review retained Bulgaria on the Watch List. Over the past few years, there has been a steady resurgence of piracy, mainly in the sale of pirated optical disc media (ODM). Today, the level of open and massive music piracy and copyright crime on Bulgaria's domestic market is unacceptably high and enforcement at all levels is inadequate. Although industry's forensic evidence indicates that pirate facilities are operating once again in Bulgaria, the Bulgarian authorities have not adequately recognized or addressed the possibility of piracy production.

Furthermore, Bulgaria is still widely used for transshipment of pirate CDs from Ukraine and Russia to the Balkans, Greece, and Turkey. CD-R piracy has been increasing significantly, and the local music business in particular is feeling the brunt of this phenomenon.

Although Bulgarian IPR legislation is generally adequate--it includes modern patent and copyright laws and criminal penalties for copyright infringement--industry representatives believe effective IPR protection requires improvements in certain pieces of legislation, including the Penal Code and the Penal Procedure Code.

Parliament approved in September 2005 the long awaited Law on Administrative Control over the Manufacture and Distribution of ODM, which now requires SID codes on blank optical discs (OD) produced in Bulgaria and strengthens the import/export regime for raw materials and equipment involved in the ODM production. However, the new law does not allow the right holders' organizations and their representatives to participate in the inspections and excludes from the registration regime goods in transit, which sets the stage to transform Bulgaria into a transit and dispatch center of pirate production from manufacturing countries (e.g. Russia., Ukraine,) to other territories.

The new ODM law further weakens enforcement by restricting the authorities of state officials. State control bodies are not allowed to require inspection of the manufacturing facilities in operation, to seize copies of documents (contracts, raw material supply contracts, etc.), to require and seize samples of the inspected carriers and to seize raw material, manufacturing equipment, matrices, samples or ready product and documentations with the purpose of establishing facts and circumstances related to the inspection.

Yet another major drawback of the new ODM law is that persons who furnish forged documents or documents with false content are not being held liable.

The ODM law also introduces several requirements that have the potential to create serious trade barriers, according to industry representatives. The law requires that all ODs containing sound recordings or films and other audiovisual works imported to Bulgaria have a SID code which is practically impossible as in developed countries SID codes are not required.

Parliament is currently debating amendments to the 1993 Law on Copyrights and Related Rights, which will align Bulgaria's copyright legislation with the European requirements. In particular, the proposed amendments will implement two directives of the EU in the area of copyrights: Directive 2001/84/EC of the European Parliament and of the Council on the resale right for the benefit of the author of an original work of art; and Directive 2004/48/EC of the European Parliament and of the Council on the enforcement of intellectual property right. Also, the amendments will establish the mechanism regulating the administration of the newly-established database and copyright information sharing system sponsored by the EU.

Despite some successes by individual agencies, enforcement greatly suffers because of the lack of overall coordination between agencies and inadequate resources and legal loopholes. The government lacks sufficient institutional capacity and will to effectively address major enforcement problems, especially in combating and prosecuting organized crime groups.

Software piracy continues to be a serious problem, although industry legalization/enforcement campaigns have made noticeable gains against unauthorized software. Local software industry representatives report that, along with good cooperation from Bulgarian law enforcement authorities, the piracy rate has been contained to 71 percent of the products in the market in 2004. The amount of lost revenues due to piracy, however, has increased by 27 percent, from USD 26 million in 2003 to USD 33 million in 2004. The lack of actual prosecutions and court decisions has kept the piracy rate at a high level. Between October 2004-October 2005 only five criminal and one civil judgment have been ruled by the Bulgarian judiciary, but the verdicts against the offenders are inadequate and non-deterrent. Distribution of unlicensed software on computers continues and it is becoming increasingly difficult to effectively address this problem as computer resellers install unlicensed software at the customers' premises. Also, the domestic market offers enormous amounts of illegal CD-ROMs containing a full range of different pirated software. Internet distribution of illegal software is also a growing problem.

The US government has formulated an action plan, which will assist in focusing attention on immediate and effective

implementation of the new Optical Disk Media (ODM) Law and the amended Copyrights and Related Rights legislation, enforcement actions and ministerial-level coordination, designing training programs and improving efforts to address counterfeiting of U.S. spirits.

The Bulgarian government included in its 2003 drug law a provision to provide protection for confidential test data submitted for marketing approval by pharmaceutical products companies. The law, however, links data protection to a valid patent. Bulgaria joined the European Patent Convention on July 1, 2002 and has obtained observer status in the Administrative Council of the European Patent Organization.

The Association of American Pharmaceutical Companies in Bulgaria (AAPCB) has told us that the Bulgarian government's practice of shortening the patent life of innovative medical products in violations of the Bulgarian patent legislation and the TRIPS Agreement could constitute a major barrier for their exports to Bulgaria and investments. The industry has reported that in several cases generic copies of the original drugs have been granted marketing authorizations, registered retail price and applied/received access to reimbursement prior to expiration of the patent of the original pharmaceutical product.

Industry has told us that the Bulgarian government's inability to protect trademarks is a significant barrier to investment and legitimate domestic economic development. U.S. businesses have noted significant difficulties in obtaining relief against trademark infringement. Even if courts understand the law and issue orders, the entities charged with enforcement often cannot be relied upon to carry out the court judgment. Under Bulgarian law, legal entities cannot be held criminally liable. Therefore, the criminal penalties for copyright infringement and willful trademark infringement are limited.

There is evidence of significant counterfeit production in Bulgaria and illegal import of counterfeited U.S. brand distilled alcoholic spirits. Some spirits companies have estimated that almost 10 percent of the products sold in the Bulgarian market may be counterfeit.

SERVICES BARRIERS

As in other EU candidate countries, Bulgaria's 1998 Radio and Television Law requires a "predominant portion" of certain programming to be drawn from European-produced works and sets quotas for Bulgarian works within that portion. This requirement, however, is only to be applied to the extent "practicable." Foreign broadcasters transmitting into Bulgaria must have a local representative, and broadcasters are prohibited from entering into barter agreements with television program suppliers.

INVESTMENT BARRIERS

The U.S.-Bulgaria Bilateral Investment Treaty (BIT) took effect in 1994 and provides guarantees for U.S. investors of both national and MFN treatment, the right to make financial transfers freely and without delay, international law standards for expropriation and compensation, and access to binding international arbitration. In 2003, to address several actual and potential incompatibilities between BIT obligations and EU law, the United States exchanged interpretive notes with the governments of Bulgaria and seven other European countries expected to join the EU over the next few years. The United States and the prospective EU Member States also agreed to make several narrow amendments to the texts of the relevant BITs. Both the United States and Bulgaria have ratified the BIT amendments, but the amendments will not enter into force until Bulgaria joins the EU.

The 2005 property rights constitutional amendment, which comes into effect on January 1, 2007 and will lift the existing ban prohibiting foreigners to buy land in Bulgaria, favors EU over U.S. investors. While EU citizens and entities will be allowed to acquire property directly by virtue of Bulgaria's accession treaty, all other foreigners will be able to do so only on the basis of an international agreement ratified by the Bulgarian Parliament. In the meantime, the constitutional prohibition against ownership of land by foreign individuals remains in force. However, foreign-owned companies registered in Bulgaria are considered to be Bulgarian persons. U.S. owned companies that register in Bulgaria therefore may acquire land in Bulgaria.

Local companies in which foreign partners have controlling interests must obtain prior approval (licenses) to engage in certain activities: production and export of arms/ammunition; banking and insurance; exploration, development, and exploitation of natural resources; and acquisition of property in certain geographic areas. There

are neither specific export-performance requirements nor specific restrictions on hiring expatriate personnel, although residence permits are often difficult to obtain.

A recent Bulgarian law eliminated the withholding tax on dividends for European investors, but U.S. investors face a withholding tax of 15 percent.

FOREIGN TRADE BARRIERS

New insolvency rules in Bulgaria's Commercial Code and its Law on Public Offering of Securities have greatly improved the legislative protection for minority shareholders. However, enforcement of the law's provisions is inadequate and corporate governance remains weak.

In 2003, Parliament approved a new Telecommunications Law which increases institutional and regulatory liberalization of the Bulgarian telecommunications sector but focuses more on institutional issues and the protection of state interests than on greater market liberalization. The new Telecommunication Act extended until December 2005 the Bulgarian Telecommunications Company's (BTC) control over the sole telecommunication network.

A June 1999 law regulating gambling imposes additional requirements on foreigners organizing games of chance. Foreigners can receive a license to establish a casino in a hotel only if they satisfy one of the following conditions: (1) purchase or construction of a hotel rated four-star or higher; or (2) investment of at least \$10 million and employment of at least 500 workers in economic activities unrelated to gambling.

According to U.S. businesses, other steps needed to improve the environment for foreign investment include improved creditor rights through improvements to bankruptcy law and procedures; reform of the judicial system; improved accounting standards and risk assessment; reform of the energy sector; and transparency and accountability in public policy to reduce the perception of corruption.

ELECTRONIC COMMERCE

Bulgaria's Law on the Electronic Document and Electronic Signature went into effect in 2001. Three implementation ordinances for this law aimed at improved access to information services and promotion of electronic commerce were approved in 2002: Ordinance on Requirements for Algorithms for Advanced Electronic Signature; Ordinance for Activity of Certification-Service-Providers, Termination Procedure, and Requirements for Provision of Certification Services; and Ordinance for the Order of Registration of Certification-Service-Providers.

OTHER BARRIERS

Selective enforcement
Foreign investors complain that tax evasion by private domestic firms combined with the failure of the authorities to enforce collection from large, often financially-precarious, state-owned enterprises places the foreign investor at a disadvantage. The multiplicity of Bulgarian licensing and regulatory regimes, their arbitrary interpretation and enforcement by the bureaucracy, and the incentives this creates for corruption, have long been seen as an impediment to investment, private business development and market entry. The 2003 Restriction of Administrative Regulation and Control of Economic Activity Act is expected to considerably lighten the potential of regulatory abuse at all levels of government, and when implemented, should improve the overall business environment.

Execution of judgment

Bulgarian and foreign observers caution that the proceedings for the execution of judgments under the Code of Civil Procedure remain slow and unpredictable. Also, the civil servants who are currently responsible for carrying out execution are viewed as extremely inefficient. Thus, problems are procedural, as well as systemic. Further reform of the legal framework and its implementation will be needed. In May 2005, Bulgaria addressed the systemic issues by adopting the Private Execution Agents Act, which created private execution agents to work in parallel with the state officials. The private execution agents are expected to become operational in 2006. However at this early stage of reform it is unclear whether it will be able to effectively address the current problems. Procedural impediments to execution of judgments still remain to be addressed through amendments to the Code of Civil Procedure.

The U.S. does not currently have reciprocity with Bulgaria, so Bulgarian courts are not obliged to honor decisions of U.S. courts. In practice, enforcement of foreign judgments, as well as their execution, is subject to delays, sometimes

resulting from corruption and inefficiency in the judicial system.

Access to international arbitration

There are opportunities for international arbitration in Bulgaria. The Code of Civil Procedure mandates that foreign court of arbitration is possible only if at least one of the parties has its seat or residence abroad. As a result, foreign-owned, Bulgarian-registered companies having a dispute with a Bulgarian entity can only have arbitration in Bulgaria. However, under the Law on the International Commercial Arbitration, the arbitrator himself could be a foreign person. Under the same act, the parties can agree on the language to be used in the arbitration proceedings. The major and most experienced arbitration institution is the Arbitration Court of the Bulgarian Chamber of Commerce and Industry (BCCI).

Not all disputes, however, may be resolved through arbitration. Disputes regarding rights over real estate properties in the country or labor disputes can only be heard by the courts. Additionally, Bulgarian courts have exclusive competence over industrial property disputes regarding patents issued in Bulgaria.

Bulgaria is a party to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention), which facilitates enforcement of foreign arbitral awards. However, having gone through the enforcement proceedings before the Bulgarian courts, the creditor needs then to execute the award using the general framework for execution of judgments in the country, which is inefficient.

Mediation

Businesses wishing to use mediation to solve their disputes in Bulgaria may find it hard to select experienced mediators. This service has just started to develop in the country following the adoption at the end of 2004 of the Mediation Act. BCCI and the American Chamber of Commerce (AmCham) responded promptly by opening commercial mediation centers. The mediators at these centers have been trained with US assistance but at this point lack sufficient experience to be able to provide high quality mediation services.

Textiles and apparel

As of January 1, 2002, Bulgaria eliminated all tariffs for industrial imports from the EU under its association agreement with the European Union, including textiles and apparel. Under Protocol One on Textile and Clothing Products of the European Agreement, the EU eliminated quotas on textile and clothing products originating in Bulgaria on January 1, 1998, and eliminated tariffs on textile and clothing products on January 1, 1997. Bulgaria levies tariffs on textile and apparel from the United States, but does not impose any quantitative restrictions (quotas) on imports from the United States.

BEYRLE